

**DOMESTIC PROXY VOTING GUIDELINES
LOS ANGELES COUNTY EMPLOYEES
RETIREMENT ASSOCIATION**



APRIL 22, 2009

**Guidelines Are Derived in Large Part From the
RiskMetrics Group Proxy Voting Manual**

Introduction

The domestic proxy voting guidelines contained in this document are designed to provide guidance to investment staff when voting proxies on behalf of the Board of Investments and the plan participants of the Los Angeles County Employees Retirement Association (LACERA).

RiskMetrics Group (RMG) and Glass Lewis & Company are LACERA's proxy voting advisors. RMG,¹ LACERA's principal proxy advisor, provides investment staff with corporate governance research and analysis, and proxy voting recommendations for annual and special meetings of publicly-held U.S. companies. LACERA's proxy voting guidelines are based in large part on RMG's Proxy Voting Manual. Glass Lewis provides staff with supplemental research, analysis, and proxy voting recommendations.

The guidelines are divided into eleven sections:

- I. The Board of Directors
- II. Contested Elections
- III. Takeover Defenses
- IV. Miscellaneous Corporate Governance Provisions
- V. Capital Structure
- VI. Executive and Director Compensation
- VII. State of Incorporation
- VIII. Mergers and Corporate Restructuring
- IX. Auditors
- X. Social and Environmental Issues
- XI. Other Issues

Each section addresses the most common types of proxy voting issues in that specific category. Each section also indicates whether the voting issues discussed appear in proxy statements as management proposals, shareholder proposals, or as both. LACERA's proxy voting recommendations--for, against, or case-by-case--are listed in underlined, boldface type.

In all cases, when voting LACERA proxies, staff and/or proxy advisor are obligated to evaluate the financial impact of the issues. All votes must be cast for the exclusive benefit of plan participants and beneficiaries. All votes must be made with a view to maximize the long-term value of plan holdings.

¹ RMG also provides staff with research, analysis, and recommendations for voting environmental and social responsibility issues.

On August 27, 2007, the Board of Investments created a new Corporate Governance Committee (CGC) comprised of four Board members. This committee replaces the original management-based CGC established in March 2003. Section XI discusses the authority of the Corporate Governance Committee: 1) to instruct the investment staff to cast votes on certain shareholder proposals, and 2) addresses other actions the Committee may take with respect to the voting of proxies.

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I. Board of Directors

Although the election of directors is a customary voting item at all corporate annual meetings, electing directors is still considered to be the most important stock ownership right that institutional shareholders can exercise. Directors oversee the management of a corporation and make decisions on the most important issues including the hiring and, if necessary, firing of the CEO, restructuring, the sale of major assets, mergers, acquisitions, and, in the event of a bid, the sale of the company.

Generally, the practice of electing directors rarely allows a shareholder any choice in the voting process. In most cases, the option recommended to shareholders is a blanket endorsement of a slate of management nominees.

Given that most directors fulfill their fiduciary obligations exceptionally well, most of management's recommendations should be supported. However, when available information confirms a poor performance record for specific nominees, shareholders should withhold votes from those candidates.

A. Voting on Director Nominees in Uncontested Elections

➤ LACERA votes for/against director nominees on a case-by-case basis. The following factors should be examined when evaluating nominees for election as director:

1. Long-term corporate performance record relative to a market index;

- Long term increases in shareholder wealth – total shareholder returns relative to a standard industry peer group and appropriate market index (1, 3 and 5 years).
- Earnings-based performance – return on shareholder equity (1, 3 and 5 years).
- Financial Strength – changes in S&P common stock ranking.

2. Majority of Independent Directors

Independent outside directors can bring objectivity and a new perspective to the numerous issues facing a corporation. They also bring new contacts and specialized skills to a board of directors. When formulating executive compensation policies and responding to takeover offers, the inherent conflict of interest problem is much less severe for outsiders than it is for executive officers.

- LACERA votes for shareholder proposals requiring that the board consist of a majority or substantial majority (two-thirds) of independent directors unless the board composition already meets the proposed threshold (by RMG's definition of independence).

- LACERA votes **for** shareholder proposals requiring the board audit, compensation, and/or nominating committees be composed exclusively of independent directors if they currently do not meet that standard.
- LACERA votes **withhold** from insiders and affiliated outsiders sitting on the audit, compensation, or nominating committees.
- LACERA votes **withhold** from insiders and affiliated outsiders on boards that are lacking any of these three panels.
- LACERA votes **withhold** from insiders and affiliated outsiders on the board where the full board is less than majority independent.
- LACERA votes **withhold** from members of the compensation committee when there is a negative correlation between chief executive pay and company performance

Directors Definitions²

Inside Director

- Employee of the company or its affiliates (subsidiary, sibling company, or parent company).
- Non employee officer³ of the company if among the five most highly compensated individuals.
- Section 16 officer⁴
- Interim CEO.
- Beneficial ownership⁵ of more than 50 percent of the company's voting power (this may be aggregated if voting power is distributed among more than one member of a defined group; e.g., members of a family beneficially own less than 50 percent individually, but combined own more than 50 percent).

Affiliated Outside Director

- Board attestation that an outside director is not independent.
- Former CEO of the company or its affiliate.
- Former interim CEO if the service was longer than 18 months. If the service was between twelve and eighteen months, then an assessment of the interim CEO's employment agreement will be made.

² Source: Risk Metrics Group, Corporate Governance Policy 2005 Updates.

³ According to RMG, an example of a non employee officer is when the Chairman of the Board is not an employee of the company.

⁴ Officers subject to Section 16 of the Securities and Exchange Act of 1934 include the chief executive, operating, financial, legal, technology, and accounting officers of a company (including the president, treasurer, secretary, controller, or any vice president in charge of a principal business unit, division or policy function).

⁵ RMG definition of beneficial ownership: A shareholder that exercises direct voting rights and accrues economic value from holding those shares.

- Former executive of the company, an affiliate or an acquired firm within the past five years.
- Executive of a former parent or predecessor firm at the time the company was sold or split off from the parent/predecessor within the last five years.
- Executive, former executive, general or limited partner of a joint venture or partnership with the company.
- Relative of a current employee of company or its affiliates (relative follows the SEC definition of “immediate family members” which covers: spouses, parents, children, step-parents, step-children, siblings, in-laws, and any person sharing the household of any director, nominee for director, executive officer, or significant shareholder of the company).
- Relative of a current Section 16 officer of company or its affiliates.
- Relative of former Section 16 officer, of company or its affiliates within the last five years.
- Currently provides (or a relative provides) professional services directly to the company, to an affiliate of the company or an individual officer of the company or one of its affiliates in excess of \$10,000 per year.
- Employed by (or a relative employed by) a significant customer or supplier (if the company makes or receives annual payments exceeding the greater of \$200,000 or five percent of the recipient’s (the party receiving the financial proceeds from the transaction) gross revenues).
- Has (or relative has) any transactional relationship with the company or its affiliates, excluding investments in the company through a private placement.
- Any material financial tie or other related party transactional relationship to the company.
- Has a contractual/guaranteed board seat and is party to a voting agreement to vote in line with management on proposals being brought to shareholders.
- Has (or relative has) an interlocking relationship as defined by SEC involving members of the board of directors or its Compensation and Stock Option Committee.
- Founder of company but not currently an employee.
- Is (or relative is) a trustee, director, or employee or a charitable or non-profit organization that receives grants or endowments from the company or its affiliates.

Independent Outside Director

- No material connection to company other than board seat (Material is defined as a standard of relationship (financial, personal or otherwise) that a reasonable person might conclude could potentially influence one’s objectivity in the boardroom in a manner that would have a meaningful impact on an individual’s ability to satisfy requisite fiduciary standards on behalf of shareholders).

3. Composition key board committees;

- LACERA votes **for** shareholder proposals that request that the board audit, compensation and/or nominating committees include independent directors exclusively.
- LACERA votes **withhold** from any director nominees if the board has failed to establish a nominating, compensation, or audit committee, solely comprised of independent directors.

4. Nominee's attendance at meetings;

- LACERA votes **withhold** from any director nominee who attended less than 75 percent of the board and committee meetings without a valid excuse, such as illness, service to the nation, work on behalf of the company, or funeral obligations.

5. Corporate governance provisions and takeover activity;

- LACERA votes **withhold** from director's nominees if the director has implemented or renewed a dead-hand or modified dead-hand poison pill without shareholder approval.⁶
- LACERA votes **withhold** from any director who has failed to act on takeover offers where the majority of the shareholders have tendered their shares.
- LACERA votes **withhold** for all director nominees that have not implemented a shareholder proposal that was approved by a majority of the votes cast after one year of Board inaction.
- LACERA votes **withhold** from directors who enact egregious corporate governance policies or fail to replace management as appropriate.
- LACERA votes **withhold** from directors who are inside directors and sit on the audit, compensation or nominating committees.
- LACERA votes **withhold** from directors who sit on the audit committee if;
 - Non-audit fees paid to the auditor are excessive.
 - The company receives an adverse opinion on the company's financial statements from its auditor.
 - There is persuasive evidence that the audit committee entered into an inappropriate indemnification agreement with its auditor that limits the ability of the company, or its shareholders, to pursue legitimate legal recourse against the audit firm.
- LACERA votes **withhold** from directors who sit on the compensation committee, and;
 - There is a negative correlation between the chief executive's pay and company performance.
 - The company reprices underwater options for stock, cash or other consideration without prior shareholder approval, even if allowed in their equity plan.

⁶ A dead hand poison pill is particularly egregious because it prohibits any directors, other than continuing directors, from removing the pill, thus disenfranchising future directors.

- *The company fails to submit one-time transfers of stock options to a shareholder vote.*
- *The company fails to fulfill the terms of a burn rate commitment they made to shareholders.*
- *The company has practiced options backdating - depending on the severity. This includes committee members who oversaw the questionable options grant practices or current committee members who fail to respond to the issue proactively based upon the following factors:*
 - *Reason and motive for the options backdating issue; such as inadvertent versus deliberate grant date changes.*
 - *Length of time of options backdating.*
 - *Size of restatement due to options backdating.*
 - *Corrective actions taken by the board or compensation committee; such as canceling or repricing backdated options or the recoupment of option gains on backdated grants.*
 - *Adoption of a grant policy that prohibits backdating and creation of a fixed grant schedule or window period for equity grants going forward.*
- *LACERA votes **against/withhold** from compensation committee members, CEO, and potentially the entire board, if the company has poor compensation practices. Examples of poor pay practices are:*
 - *Egregious employment contracts.*
 - *Excessive perks/tax reimbursements.*
 - *Abnormally large bonus payouts without justifiable performance linkage or proper disclosure.*
 - *Egregious pension/SERP (Supplemental Executive Retirement Plan) payouts.*
 - *New CEO with overly generous new hire package.*
 - *Excessive severance and/or change in control provisions.*
 - *Dividends or dividend equivalents paid on unvested performance shares or units.*
 - *Poor disclosure practices.*
 - *Internal pay disparity.*
 - *Options backdating.*
 - *Other excessive compensation payouts or poor pay practices at the company.*
- *LACERA votes **for** shareholder proposals seeking disclosure of information regarding the company, board, or compensation committee's use of compensation consultants, such as consultants name, business relationship(s) and fees paid.*
- *LACERA votes **against** proposals if the compensation committee does not fully consist of independent outsiders.*

6. Excessive Directorships

The number of board positions a director holds is of importance and should be taken into consideration when voting on a director nominee. While CEO's benefit from their exposure to other company boards, the time demands of their full-time jobs limit the number of outside commitments they can manage without compromising their effectiveness as CEO's and as outside directors.

- LACERA votes ***withhold*** from directors who are CEO's of publicly-traded companies who serve on more than three public boards, i.e., more than two public boards other than their own board.
 - Withhold votes will apply only to their outside directorships and not at the company in which they presently serve as CEO.
- LACERA votes ***withhold*** from all other directors who serve on more than six public company boards.
 - LACERA does not differentiate between directors who have full time jobs and those who are retired, "professional" directors.

7. Interlocking directorships

There is a degree of value added by interlocking directorships from coordination of business activities. However, the relationship between interlocking directorships should be carefully examined, as there is the potential for objectivity to get lost amid the personal relationship shared by the interlocking directors, thus causing shareholder interests to suffer.

B. Voting on Provisions Affecting Director Elections

1. Term of Office

A requirement limiting office terms could conceivably harm shareholder interests by forcing experienced and knowledgeable directors off the board. Shareholders should, instead, retain the ability to evaluate and cast their vote on all director nominees once a year.

- LACERA votes ***against*** shareholder proposals to limit the tenure of outside directors.

2. Stock Ownership Requirements;

Corporate directors should own some amount of the stock of the companies for which they serve as director. This is an effective way for director and shareholder interests to be aligned. However, many highly qualified individuals might not be able to meet this requirement--academics and members of religious orders, for example. Imposing an across-the-board minimum ownership requirement could therefore prevent these nominees from serving as directors.

- LACERA votes ***against*** shareholder proposals requiring directors to own a minimum amount of company stock in order to qualify as a director, or to remain on the board.

3. Age limits

- LACERA votes ***against*** shareholder proposals to impose mandatory retirement age for outside directors.

4. Whether a retired CEO sits on the board

The presence of a retired CEO remaining on the board may limit the new CEO's ability to assume control in order to be an effective leader. Factors which could justify the election of a retired CEO are;

- The chairman of the board and board nominating committee are independent directors.
- Shareholders have the power to effect governance changes.
- A strong performance record or aggressive response to poor market conditions

5. Separation of CEO and Chairman

A 1991 study⁷ concluded that companies with independent governance (Chairman and CEO are not the same person) consistently outperformed companies with Chairman/CEO duality in terms of return on investment, return on equity and profit margin. Nevertheless, the duality issue should be reviewed on a case-by-case basis because many small firms with a limited roster of executive officers may find it necessary to combine these positions.

- LACERA generally votes *for* shareholder proposals that would require the position of chairman be filled by an independent director unless there are compelling reasons to recommend against the proposal, such as a counterbalancing governance structure, which may include any of the following:

Designated lead director, elected by and from the independent board members, with clearly delineated duties. (The role may alternatively reside with a presiding director, vice chairman or rotating lead director). At a minimum these should include:

- Presides at all meetings of the board at which the chairman is not present, including executive sessions of the independent directors.
- Serves as liaison between the chairman and the independent directors.
- Approves information sent to the board.
- Approves meeting agendas for the board.
- Approves meetings schedules to assure that there is sufficient time for discussion of all agenda items.
- Has the authority to call meetings of the independent directors.
- If requested by major shareholders, ensures that he is available for consultation and direct communication.
- 2/3 independent board.
- All independent key committees.
- Established governance guidelines.

⁷ P.L. Rechner and D.R. Dalton, "CEO Duality and Organizational Performance: A Longitudinal Analysis," Strategic Management Journal, Vol. 12 pp. 155-60 (1991).

- The company should not have underperformed its peers and index on a one-year and three-year basis, unless there has been a change in the Chairman/CEO position within that time.
- The company does not have any problematic governance issues.

6. Majority vote standard.

Under most state corporate laws, including Delaware’s statutes, a plurality vote is the standard used in the election of the board of directors. Under a plurality system, a board-backed nominee in an uncontested election needs to receive only a single affirmative vote to claim his or her seat in the boardroom. Even if holders of a substantial majority of the votes cast “withhold” support, the director nominee still “wins” the seat.

Under the majority vote standard, a director nominee must receive support from holders of a majority of the proxy votes cast in order to be elected (or re-elected) to the board. A majority vote standard transforms the director election process from a symbolic gesture to a meaningful voice for shareholders.

- *LACERA votes for shareholder proposals requesting the Board to amend the Company’s governance documents (certificate of incorporation or bylaws) to provide that director nominees shall be elected by the majority of proxy votes cast at the annual shareholder meeting.*

7. Nominee qualifications.

Proposals should have reasonable criteria and analyzed to identify to what extent they may preclude dissident nominees from joining the board.

- *LACERA votes case-by-case on shareholder proposals that establish or amend director qualifications.*
- *LACERA votes against shareholder proposals requiring two candidates per board seat.*

II. Voting on Director Nominees in Contested Elections

A. Proxy Contests

(1-5) Consideration factors

B. Reimbursement of Proxy Solicitation Expenses

II. Voting for Director Nominees in Contested Elections

1. Proxy Contests

Proxy contests occur when shareholders are solicited (to influence their voting,) by two separate groups at annual or special meetings of a corporation. Generally, one group represents management and the other represents a dissident or group of dissidents that own a significant equity position in the company.

In most cases, the dissident group has unsuccessfully attempted to convince management that various changes need to be made, such as corporate restructuring, raising a stock dividend or making a strategic acquisition. Frustrated by unsatisfactory total returns and management's failure to achieve other financial benchmarks, the group launches a proxy contest.

A proxy contest may involve the election of an entire slate of board members, in which case the dissidents' goal is to take control of the company by replacing all board members and ultimately ousting members of the incumbent management team. A proxy contest may also involve the election of a minority of board seats, whereby dissidents seek a strong enough position in a company to change corporate strategy without necessarily changing control.

Contested elections frequently result in new management and major shifts in corporate strategy. Consequently, proxy contests are of critical importance to a shareholder. Recent studies indicate that dissidents in proxy contests—even when failing to gain board seats—often accomplish at least some of their objectives.

- *Votes in a contested election of directors are evaluated on a case-by-case basis, considering the following factors:*

In addition to reviewing the criteria in Part I - "Voting on Director Nominees in Uncontested Elections." The following factors should be taken into consideration when voting on contested elections for director nominees:

- Overall long-term financial performance of the target company relative to its industry. Key measures include five-year annual compound growth rates for sales, operating income, net income, and total shareholder returns (share price appreciation plus dividends). Other financial indicators include margin analysis, cash flow, and debt levels.
- Management's track record. Review of strategic decision making such as acquisition record, new business development, effectiveness of marketing campaign, and strategic positioning. Look for actions that show a blatant disregard for shareholders such as a blocked takeover bid that shareholders may have been interested in accepting.

Consider executive pay and spending on perks, particularly in conjunction with sub par performance and employee layoffs.

- Background to the proxy contest. Chronology of events leading up to the proxy contest. Look for evidence to indicate that the dissidents attempted to work cooperatively with management on the issues in question. Also look closely at how quickly and in what manner management responds to the dissidents' concerns.
- Qualifications of director nominees-both slates. For incumbent slate, board and key committee composition is emphasized. Includes review of knowledge and experience of incumbents. Also includes a review of the corporate governance profile looking for entrenchment devices that reduce accountability. For the dissident slate, each candidate's knowledge and experience of the target company and industry is reviewed, as well as the nominees' track record at other companies.
- Evaluation of what each side is offering shareholders as well as the likelihood that the proposed objectives and goals can be met. Look for a clear strategic operating plan from both management and the dissidents. Optimistic projections must be backed up with a realistic plan for achieving goals.
- Stock ownership positions. Substantial share ownership enhances the credibility of director nominees. In the case of dissident nominees, an outstanding tender offer also serves to enhance credibility. When there is an outstanding tender offer, the proxy contest is considered to be a tactic to enhance the offer, and the offer itself is also analyzed.

2. Reimburse Proxy Solicitation Expenses

Most of the expenses incurred by incumbents in a proxy contest are paid directly by the company. Conversely, dissidents are typically reimbursed only for proxy solicitation expenses, if they gain control of the company. Sometimes, where the board and a majority of shareholders approve, the dissidents who have only gained partial representation will also be reimbursed. In successful proxy contests, new management will often seek shareholder approval for the use of company funds to reimburse themselves for the costs of proxy solicitation.

- *Decisions to provide full reimbursement for dissidents waging a proxy contest are made case-by-case.*
- *In cases where LACERA supports the dissident position, we would vote for the reimbursement of reasonable expenses.*

III. Takeover Defenses

- A. Proxy Contest Defenses
 1. Board Structure: Staggered vs. Annual Elections
 2. Shareholder Ability to Remove Directors
 3. Cumulative Voting
 4. Shareholder Ability to Call Special Meetings
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- B. Tender Offer Defenses
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 4. Dual Class Authorization / Unequal Voting Rights
 5. Supermajority Voting Requirements
 6. White Squire Placements

III. Takeover Defenses

Takeover defenses are designed to make it more difficult to change control of a corporation's management. The management of companies that ask shareholders to approve various anti-takeover provisions usually state that these measures are intended to protect shareholders, either by deterring efforts to change control or by giving management stronger defenses if an unsolicited proxy contest or tender offer occurs. However, these proposals tend to transfer rights or powers from shareholders to management. Once shareholders transfer the right to decide who will manage a company, they are unlikely to regain these rights.

A. Proxy Contest Defenses

1. Board Structure: Staggered (classified) vs. Annual Elections

A classified board is generally divided into three separate classes, with one class of directors elected each year, thus providing for "staggered" terms. Because only a minority of the directors are elected each year, dissident shareholders are unable to win control of the board (by proxy contest) in a single election. Two years would be necessary to gain majority control and three years to gain full control.

- LACERA votes ***against*** proposals to classify the board.
- LACERA votes ***for*** proposals to repeal classified boards and to elect all directors annually.

2. Shareholder Ability to Remove Directors

Shareholder ability to remove directors, with or without cause, is either prescribed by a state's business corporation law, a company's articles of incorporation, or its bylaws. If state law does not specify removal procedures, it is left to the company to determine that process.

Removal of directors only for cause requires proof of self-dealing, fraud or misappropriation of corporate assets. By requiring that "cause" be demonstrated in the removal process, management insulates directors from removal by shareholders even if the director has demonstrated poor performance, not attended meetings, or has not acted in the best interest of the shareholders.

If a company's bylaws do not specify terms for removal, it should be assumed that directors may be removed without cause. Removal without cause allows shareholders to remove a director by a majority vote before his/her term expires.

- LACERA votes ***against*** proposals that provide that directors may be removed only for cause.
- LACERA votes ***for*** proposals to restore shareholder ability to remove directors with or without cause.
- LACERA votes ***against*** proposals with provisions stating that only continuing directors may elect replacements to fill board vacancies.
- LACERA votes ***for*** proposals that permit shareholders to elect directors to fill board vacancies.

3. Cumulative Voting

Most corporations provide that shareholders are entitled to cast one vote for each director for each share owned. Some companies allow cumulative voting for directors. This permits shareholders to distribute the total number of votes they have, in any manner they wish, when electing directors.

For example, a shareholder who owns 1,000 shares of stock in a company that is electing 10 directors will normally cast 1,000 votes for each of the 10 directors. However, with cumulative voting, the shareholder can distribute the total number of votes (10 X 1,000 =10,000) to one candidate or several candidates if they wish.

- LACERA votes ***against*** proposals to eliminate cumulative voting.
- LACERA votes ***for*** proposals to permit cumulative voting in accordance with the California Government Code § 6900.

§ 6900. Cumulative voting; "Governmental body"

Whenever any governmental body is a shareholder of any corporation, and a resolution is before the shareholders which will permit or authorize cumulative voting for directors, such governmental body shall vote its shares to permit or authorize cumulative voting.

As used in this section the term "governmental body" means the state, and any office, department, division, bureau, board, commission or agency thereof, and all counties, cities, districts, public authorities, public agencies and other political subdivisions or public corporations in the state.

4. Shareholder Ability to Call Special Meetings

Nearly all state corporation statutes allow shareholders to call a special meeting when they want to take action on certain matters that occur between regularly scheduled annual meetings. However, shareholders may lose this important right--the ability to remove directors or initiate a shareholder resolution without having to wait for the next scheduled meeting--if management places some form of restriction on that right.

- LACERA votes ***against*** proposals to restrict or prohibit shareholder ability to call special meetings.
- LACERA votes ***for*** proposals that remove restrictions on the right of shareholders to act independently of management.

5. Shareholder Ability to Act by Written Consent

Consent solicitation can be advantageous to both shareholders and management because the process does not involve the expense of holding a physical meeting. A consent solicitation is mailed to shareholders for their vote and signature (similar to proxy solicitation), and delivered to management.

Limitations on written consent are clearly contrary to shareholder interests. In terms of day-to-day governance, shareholders may lose the ability to remove directors or initiate a shareholder resolution without having to wait for the next scheduled meeting, if they are unable to act by written consent.

- LACERA votes ***against*** proposals to restrict or prohibit shareholder ability to take action by written consent.
- LACERA votes ***for*** proposals to allow or make easier shareholder action by written consent.

6. Shareholder Ability to Alter the Size of the Board

Proposals that allow management to increase or decrease the size of the board at its own discretion are often used by companies as a takeover defense. Shareholders should support management proposals to fix the size of the board at a specific number of directors, thereby preventing management (when facing a proxy contest) from increasing the size of the board without shareholder approval.

- LACERA votes ***for*** proposals that seek to fix the size of the board.
- LACERA votes ***against*** proposals that give management the ability to alter the size of the board without shareholder approval.

B. Tender Offer Defenses

1. Poison Pills

Poison pills have become a favorite tender offer defense of hundreds of companies in recent years. The term poison pill, also known as a shareholder rights plan, is used to describe takeover defenses that do one or more of the following. (1) Dilute the acquirer's equity holdings in the target company. (2) Dilute the acquirer's voting interests in the target company. (3) Dilute the acquirer's equity holdings in the post-merger company. Poison Pills accomplish these tasks by issuing rights or warrants to shareholders that are essentially worthless unless triggered by a hostile acquisition attempt.

The two most common poison pills are the flip-over plan and an ownership flip-in provision. The flip over plan distributes rights to share holders to purchase discounted shares of the acquirer's holdings in the post-merger company (typically at 50% of the fair market value.) The flip-in provision gives the shareholders, except the acquirer, the right to purchase discounted shares of their own company should the acquirer surpass a specified ownership threshold (typically between 20% and 50%.

Poison pills are sometimes used to bargain for a higher price when a company becomes a takeover target. However, they tend to deter offers or defeat offers rather than increase the price offered by the acquirer.

- LACERA votes **for** shareholder proposals that ask a company to submit its poison pill for shareholder ratification.
- LACERA votes **for** shareholder proposals to redeem a company's poison pill.
- LACERA reviews **case-by-case** management proposals to ratify a poison pill.
- LACERA considers supporting a proposed poison pill only if the following factors are present:
 - A 20% or higher flip-in
 - Two to three year sunset provision
(Permits shareholders to reaffirm or redeem a pill)
 - No dead-hand or no-hand features
(A dead-hand provision prohibits any directors, other than continuing directors, from removing the pill)
 - Shareholder redemption feature
90 days after an offer is announced, if the board refuses to redeem the pill, ten percent of the shares may call a special meeting or seek a written consent to vote on rescinding the pill.

➤ LACERA votes withhold/against the entire board of directors, except for new nominees who should be considered on a case-by-case basis) if any of the following apply:

- The board adopts or renews a poison pill without shareholder approval
- The board does not commit to putting it to shareholder vote within 12 months of adoption (or in the case of a newly public company, does not commit to put the pill to a shareholder vote within 12 months following the IPO)
- The board reverses itself on a commitment to put the pill to a vote.

2. Fair Price Provisions

Fair price provisions, usually found in a company's charter, require anyone wishing to purchase control of a company to pay all shareholders a defined fair price. A fair price is usually defined as the highest price that a potential acquirer pays to any shareholder during a specified period of time. Fair price requirements are intended to deter two-tiered, front-end-loaded tender offers, in which shareholders who tender (sell) their shares first receive a higher price for their shares than other shareholders.

- LACERA votes against proposals to raise the shareholder vote requirements greater than a majority of disinterested shares in existing fair price provisions.
- LACERA votes for shareholder proposals to lower the shareholder vote requirement in existing fair price provisions.
- LACERA votes case-by-case to adopt fair price provisions. In evaluating the acceptability of such provisions the following issues need to be reviewed:
 - Whether a supermajority vote is required to overcome a board's opposition to an acquisition.
 - Whether a supermajority vote is required to appeal or amend a fair pricing provision.
 - What is the size of the block of shares controlled by officers, directors and their affiliates?
 - Whether the company maintains numerous other takeover defenses such as poison pill provisions or a classified board.
 - Whether the company has a history of rejecting premium acquisition offers.

3. Greenmail

Greenmail refers to corporate management's practice of repurchasing the shares of a potential acquirer at an above market price in exchange for the acquirer's agreement to refrain from attempts to acquire the company. The term derives from blackmail, with green substituted for black to emphasize the large sums of money often involved.

Greenmail has become so disreputable that few firms are willing to make outright payments of greenmail. Payment of greenmail may be disguised, however, by structuring exchanges, buybacks and spin-offs so that they bestow windfall gains on potential acquirers who agree not to acquire a company. This attempt to hide the true nature of their transaction is called "pale greenmail."

- LACERA votes **for** proposals to adopt anti-greenmail charter or bylaw amendments or otherwise restrict a company's ability to make greenmail payments.
- LACERA reviews **case-by-case** anti-greenmail proposals when they are bundled with other charter or bylaw amendments.

4. Dual Class Authorization/Unequal Voting Rights

Dual class authorization refers to the creation of a second class of common stock, also called class B common or special common stock. Class B common stock may have voting rights and dividend preferences that are different from the existing class of common stock. Generally, the new class of stock is non-transferable, which means the stock can only be sold back to the company. In addition, these shares must be converted back into shares of existing common stock before it can be sold on the market.

Many companies created dual class common stock to place voting control with a group of company insiders. As a result, in 1988, the SEC prohibited the issuance of a second class of common stock that had voting rights superior to the existing common stock. However, in 1990 a federal court reversed the ruling, stating that the SEC did not have the authority to decide this issue. After this ruling, many states adopted amendments to their corporation codes to allow boards to authorize stock with unequal voting rights.

It is extremely difficult to determine which incidents of dual class recapitalization deserve support. In order to support a dual class exchange offer, shareholders must be confident that the present value of the special dividend received in the offer equals or exceeds the short-term and long-term losses associated with holding limited voting right stock in a dual class company. Given the difficult, if not impossible, task of calculating the value of the vote at each company, each with differing specific circumstances, it is better to oppose dual class exchange offers on the grounds that they contribute to the entrenchment of management and allow for the possibility of management acquiring superior voting shares in the future.

- LACERA votes **against** dual class exchange offers.
- LACERA votes **against** dual class recapitalizations.

5. Supermajority Voting Requirements

Many state laws and most corporate charters require a majority vote of the company's shareholders to approve major actions such as mergers or amendments to a firm's charter or bylaws. In most states, this requirement can be raised to a higher level, a supermajority, if shareholder approval is obtained.

Supermajority requirements typically range from two-thirds to 80% of the outstanding shares. These requirements, often included in anti-takeover measures such as classified boards, make it extremely difficult to rescind or amend these measures after they are adopted.

- LACERA votes ***against*** management proposals to require a supermajority shareholder vote to approve charter and bylaw amendments.
- LACERA votes ***for*** shareholder proposals to lower supermajority shareholder vote requirements for charter and bylaw amendments.
- LACERA votes ***against*** management proposals to require a supermajority shareholder vote to approve mergers and other significant business combinations.
- LACERA votes ***for*** shareholder proposals to lower supermajority shareholder vote requirements for mergers and other significant business combinations.

6. White Squire Placements

A white squire placement is a takeover defense employed by placing large blocks of corporate securities or blank check preferred stock (stock without predefined voting and dividend rights) with “friendly” third parties. This stock can reside in numerous places; with a private investor, a company’s ESOP, another corporation or an investment fund. These placements can dilute existing shareholders’ equity and voting positions.

Shareholders can protect their voting positions, by adopting a policy to require shareholder approval before placing blank check preferred stock with any person or group, except in cases when such placement of shares is for the purpose of raising capital or making acquisitions, in the normal course of business.

- LACERA votes ***for*** shareholder proposals to require approval of blank check preferred stock issues for other than general corporate purposes.

IV. Miscellaneous Corporate Governance Provisions

- A. Confidential Voting
- B. Equal Access
- C. Bundled Proposals
- D. Shareholder Advisory Committees
- E. Director and officer Indemnification and Liability Protection
- F. Charitable Contributions
- G. Establishment of Corporate Board Policy on Shareholder Engagement

IV. Miscellaneous Corporate Governance Provisions

A. Confidential Voting

Confidential voting-- voting by secret ballot-- is one of the key structural issues in the proxy voting system. In a system of pure confidential voting, all proxies, ballots, and voting tabulations that identify individual shareholders are kept confidential. Only the vote tabulators and inspectors of election may examine proxies and ballots; management and shareholders are only informed of vote totals.

Confidential voting protects the privacy rights of shareholders. It shields employee-owners from possible retaliation if they vote against management's recommendation on controversial issues. It also promotes fairness in an electoral process in which management has many advantages over shareholders who seek support for independent initiatives. However, opponents say a secret ballot decreases the exchange of information between shareholders and management and could make it impossible to obtain a necessary quorum at annual meetings.

- LACERA votes ***for*** management proposals to adopt confidential voting.
- LACERA votes ***for*** shareholder proposals that request corporations to adopt confidential voting, use independent tabulators, and use independent inspectors of election as long as the proposals include the following stipulations for proxy contests: In a contested election, management is permitted to request that the dissident group honor its confidential voting policy. If the dissidents agree, the policy remains in place. If the dissidents do not agree, the confidential voting policy is waived.

B. Equal Access

Equal access proposals provide large shareholders (owners of \geq \$5 million in securities of the company) with the opportunity to discuss the merits of management's director nominees, nominate and profile director candidates, and review other management-sponsored proposals in the proxy statement.

- LACERA votes ***for*** shareholder proposals that would allow significant company shareholders equal access to management's proxy material to evaluate and propose voting recommendations regarding proxy proposals and director nominees, and to nominate their own candidates to the board.

C. **Bundled Proposals**

A bundled proposal is any proxy proposal that includes a number of separate elements. Some bundled proposals are straightforward, involving various components that belong together both logically and functionally. When a company reorganizes, for example, shareholders may be asked to vote on several major changes, including bylaw and charter amendments, asset spin-offs, and other related items.

However, some bundled proposals combine unrelated issues that should be presented as separate voting items. Companies deliberately use this strategy to manipulate the vote in order to pass a questionable proposal by bundling it with a proposal that would usually pass on its own.

- LACERA reviews case-by-case on bundled or "conditioned" proxy proposals. In the case of items that are conditioned upon each other, we examine the benefits and costs of the packaged items. In instances when the joint effect of the conditioned items is not in shareholders' best interests, LACERA votes against the proposals. If the combined effect is positive, LACERA supports such proposals.

D. **Shareholder Advisory Committees**

Shareholder advisory committees are comprised of significant shareholders (or nominees of such shareholders) and are designed to provide non-binding, advisory counsel to a company's board of directors. The primary purpose of this committee is to advise the board regarding shareholder concerns and to create a formal communication process between the company's stockholders and management.

- LACERA reviews case-by-case proposals to establish a shareholder advisory committee.

E. **Director and Officer Indemnification and Liability Protection**

When a corporation indemnifies its directors and officers, the corporation promises to reimburse them for certain legal expenses, damages, and judgments incurred as a result of lawsuits relating to their corporate actions. If a company lacks adequate insurance coverage for its directors, the firm's ability to indemnify directors for honest mistakes in business judgment is the only thing that shields directors from personal liability for expenses and damage awards. Many outside

directors would decline to serve on the board if the company would not provide sufficient insurance or the right to be indemnified.

The most frequent justification for limiting directors' liability is to attract and retain qualified directors who might be unwilling to serve on boards of directors if they were personally liable for acts of negligence.

- *Proposals concerning director and officer indemnification and liability protection are evaluated **case-by-case**.*
- *LACERA votes **against** proposals to limit or entirely eliminate director and officer liability for monetary damages for violating the "duty of care".⁸*
- *LACERA votes **against** indemnification proposals that would expand coverage beyond just legal expenses to acts such as negligence, that are more serious violations of fiduciary obligations than mere carelessness.*
- *LACERA votes **for** only those proposals that provide such expanded coverage in cases when a director's or officer's legal defense was unsuccessful if: (1) the director was found to have acted in good faith and in a manner that he reasonably believed was in the best interests of the company, and (2) only if the director's legal expenses would be covered.*

F. Charitable Contributions

Corporate charitable contributions can provide important benefits (direct and indirect) to long-term shareholders. Directly, shareholders benefit from the favorable tax treatment of charitable contributions. Indirectly, they benefit from the goodwill, support and name recognition that these contributions generate.

However, shareholders should not decide what are the most worthwhile charities for the corporation. Shareholders have differing and equally conscientious views regarding which charities the company should contribute to, and the amount of the contribution. As a result of these differences, management should determine which contributions are in the best interests of the company.

- *LACERA votes **against** shareholder proposals to eliminate, direct or otherwise restrict charitable contributions.*

⁸ The duty of care is defined as "a reasonable director standard". In other words, shareholders expect more from a director than what is expected from a regular "reasonable man". Directors are expected to behave reasonably, according to the experience and expertise a director should have. A reasonable man is not expected to be familiar with generally accepted accounting principles or earnings per share, but this knowledge is expected of a director.

G. Establishment of Corporate Board Policy on Shareholder Engagement

- LACERA votes for shareholder proposals requesting that the board establish an internal process, which may include a committee, to improve communications between directors and shareholders, unless the company has the following features:
- Established a structure that goes beyond the stock exchange requirements to facilitate communication between shareholders and members of the board.
 - Effectively disclosed information with respect to this structure to its shareholders.
 - Company has not ignored majority-supported shareholder proposals or a majority withhold vote on a director nominee.
 - The company has an independent chairman or lead director.

V. Capital Structure

- A. Common Stock Authorization
- B. Reverse Stock Splits
- C. Blank Check Preferred Stock Authorization
- D. Adjust Par Value of Common Stock
- E. Preemptive Rights
- F. Debt Restructuring
- G. Share Repurchase Programs
- H. Tracking Stock

V. Capital Structure

The management of a corporation's capital structure involves a number of key issues, including dividend policy, taxes, types of assets, opportunities for growth, ability to finance new projects internally, and the cost of obtaining additional capital. The majority of these decisions are best left to the board and senior management of the firm.

However, while a company's value depends more on its capital investment and operations than on how it is financed, many financing decisions have a significant impact on shareholders, particularly when they involve the issuance of additional common stock, preferred stock or the assumption of additional debt. Management may propose additional equity financing which may reduce an existing shareholder's ownership interest and can dilute the value of the investment. As a result, shareholders must evaluate all of management's recommended financing vehicles

A. Common Stock Authorization

Requests to authorize the issuance of additional shares of common stock, or additional shares of preferred, must be examined carefully. If the proposals have a legitimate business purpose, increasing the allocation may benefit shareholders. Proposals to implement a stock split, to pay a stock dividend, to raise new capital, to make shares available for stock option plans or to affect a merger or acquisition, usually fall into this category.

However, a request to issue large amount of additional stock with no specific business purpose given is not in the shareholders' best interest. A large block of authorized but un-issued shares can be used in a takeover defense to dilute the interest of a potential acquirer, by implementing a poison pill takeover defense. (Most poison pills require the availability of large amounts of common or preferred stock to implement the pill).

- LACERA reviews ***case-by-case***, proposals to increase the number of shares of common stock authorized for issue utilizing the following core guidelines.
 - Specific reasons/rationale for the proposed increase.
 - The dilutive impact of the request.
 - The board's governance structure and practises.
 - Risks to shareholders of not approving the request.
- LACERA votes ***against*** proposed common stock authorizations that increase the existing authorization by more than 100 percent, unless the company can present a clear and legitimate need for the excess shares.

- LACERA votes ***for*** proposals to approve a variance above prescribed share limits when a company's shares are in danger of being delisted or if a company's ability to continue to operate as a going concern is uncertain.
- LACERA votes ***for*** management proposals to increase common share authorization for stock splits or share dividend, provided that the split does not result in an excessive number of shares available for issuance.
- LACERA votes ***against*** proposals to create a new class of common stock with superior voting rights (all classes of common stock should have one vote per share).
- LACERA votes ***against*** proposals, at corporations with a dual class structure, to increase the number of authorized shares of the class of stock that has superior voting rights.
- LACERA votes ***against*** proposals to increase authorized common shares in which the stated purpose is to reserve additional shares to implement a poison pill.
- LACERA votes ***for*** proposals to create a new class of nonvoting or sub-voting common stock if:
 - It is intended for financing purposes with minimal or no dilution to current shareholders
 - It is not designed to preserve the voting power of an insider or significant shareholder.

B. Reverse Stock Splits

Regular stock splits exchange each share outstanding for multiple shares in order to lower share price to an optimal trading range. Reverse splits operate in the opposite fashion. Multiple shares are exchanged for a lesser amount to increase price.

- LACERA votes ***for*** management proposals to implement a reverse stock split, provided the reverse split proportionately reduces the company's number of shares authorized for issue.
- LACERA treats reverse stock splits that are not proportional to the number of shares authorized for issue, as a request for additional authorized shares. (See Common stock authorization in previous section.)
- LACERA Votes ***for*** management proposals to implement a reverse stock split to avoid delisting.
- LACERA votes ***case-by-case*** on proposals to implement a reverse stock split that does not proportionately reduce the number of shares authorized for issue. (LACERA treats reverse stock splits that are not proportional to the number of shares authorized for issue, as a request for additional authorized shares. See Common stock authorization in previous section.)

C. Blank Check Preferred Stock Authorization

Blank check preferred stock is a term used to describe preferred stock authorization that gives the board of directors broad discretion to establish voting, dividend, conversion or other rights for preferred stock that a company may issue. Broad discretion provides the board with the flexibility to meet changing business conditions.

However, blank check preferred stock is also perfectly suited for use as an entrenchment (anti-takeover) device. Many companies obtained shareholder approval to issue this class of stock as a result of hostile takeover activity in the mid-1980's. The ability of a board to issue a block of preferred stock with multiple voting or conversion rights to a friendly investor is a powerful takeover defense.

- LACERA votes **for** proposals to create blank check preferred stock in cases when the company expressly states that the stock will not be used as a takeover defense or to carry superior voting rights.
- LACERA votes **against** proposals that would authorize the creation of new classes of preferred stock with unspecified voting, conversion, dividend distribution, and other rights.
- LACERA reviews **case-by-case**, proposals to increase the number of authorized blank check preferred shares.
- LACERA votes **for** shareholder proposals to require approval of blank check preferred stock issued for other than general corporate purposes.
- LACERA votes **for** shareholder proposals to have blank check preferred stock placements, other than those shares issued for the purpose of raising capital or making acquisitions in the normal course of business, submitted for shareholder ratification.

D. Adjust Par Value of Common Stock

The purpose of par value stock (a fixed per share value) is to establish the maximum responsibility of a stockholder in the event that a corporation becomes insolvent. It represents the minimum amount that a shareholder must pay the corporation if the stock is to be fully paid when issued.

Since the par value of many issues is \$1 or less, proposals to reduce par value to facilitate the sale of additional stock are uncommon. However, there are still

times when companies with \$5 or \$10 par values need to lower the par value to sell additional stock.

- LACERA votes *for* management proposals to reduce the par value of common stock.

E. Preemptive Rights

Preemptive rights give existing shareholders the right to maintain their proportionate ownership interest in a company when new shares are issued. When preemptive rights are in effect, a company must offer existing shareholders the opportunity to buy new shares before additional shares are offered to the public.

- LACERA reviews *case-by-case*, proposals to create or abolish preemptive rights, evaluating the size of a company, the characteristics of its shareholder base, and the liquidity of the stock.
(Example: it would be difficult and costly to support a shareholder proposal that would require an S&P 500 company with over \$1 billion in equity held by thousands of shareholders, with no single shareholder owning more than one percent of outstanding shares, to implement preemptive rights each time it conducted a new offering.)

F. Debt Restructuring

Although the varieties of corporate refinancing plans are endless, shareholders need to be able to recognize and evaluate the different types of debt restructuring proposed in a proxy statement. Because of RMG's specific expertise in this arena, their team of analysts assist staff with the analysis of the restructuring (i.e. reverse leveraged buyouts, prepackaged bankruptcy plans, wrap plans).

- LACERA reviews *case-by-case*, proposals to increase common and/or preferred shares and to issue shares as part of a debt restructuring plan. The following issues are considered:
 - *Dilution*--How much will ownership interest of existing shareholders be reduced, and how extreme will dilution to any future earnings be?
 - *Change in Control*--Will the transaction result in a change in control of the company?
 - *Bankruptcy*--Is the threat of bankruptcy, which would result in severe losses in shareholder value, the main factor driving the debt restructuring?

- *Generally, LACERA votes **for** proposals that facilitate debt restructurings unless there are clear signs of self-dealing or other abuses.*

G. Share Repurchase Programs

Stock repurchase programs serve two main purposes which benefit shareholders. First, they serve as a more efficient vehicle for distributing cash to shareholders than paying dividends. Second, announcement of stock repurchase programs tend to result in increased returns to shareholders.

- *LACERA votes **for** management proposals to institute open-market share repurchase plans in which all shareholders may participate on equal terms.*

H. Tracking Stock

Tracking stock is a separate class of common stock that tracks the performance of an individual business unit of a company. A tracked business has no separate legal identity. It remains under the control of the parent company. Tracking shares are created through a charter amendment, subject to shareholder approval, providing for different classes of common stock of the parent company. Tracking stock does not represent legal ownership of the tracking unit's assets, but rather an equity interest in the parent company. A tracked business has no separate legal identity.

- *LACERA votes **case-by-case** on the creation of tracking stock, weighting the corporation's strategic value of the transaction, against any negative factors affecting the shareholder. The following factors are reviewed:*
 - Governance changes
 - Increase in authorized capital stock
 - Method of distribution (IPO or stock distribution)
 - Voting rights
 - Conversion terms
 - Stock option plan impact on existing shareholders
 - Available alternatives, such as spin-offs

VI. Executive and Director Compensation

- A. OBRA- Related Compensation Proposals
- B. Employee Stock Purchase Plans
- C. Shareholder Proposals to Limit Executive and Director Pay
- D. Golden and Tin Parachutes
- E. Employee Stock Ownership Plans
- F. 401(k) Employee Benefit Plans
- G. Say-on-Pay (Advisory vote on executive compensation)
- H. Golden Coffins
- I. Pay for Performance
- J. Supplemental Executive Retirement Plans (SERPs)

VI. Executive and Director Compensation

Executive compensation plans have, or should have, two major purposes: to provide incentives for superior performance and to reward such performance when it occurs. Plans that motivate and reward executives for outstanding performance are in a shareholders best interest. Plans that provide benefits regardless of performance are unlikely to align the interests of management and shareholders.

Most key decisions regarding executive management compensation are made by a company's board of directors or a special committee of the board. They approve the salary paid to top executives, award bonuses, and establish incentive plans that may include stock option plans and long-term performance plans. In addition, the board must review and approve supplemental compensation plans for rank-and-file employees, including employee saving plans and employee stock ownership plans (ESOP).

The rules of the New York Stock Exchange require that companies obtain shareholder approval for stock option plans, and federal tax laws require shareholder approval for qualified stock option plans. Although not required, many companies submit ESOPs for shareholder approval.

Compensation of top executives has become a national issue in recent years. In October 1992, the Securities Exchange Commission adopted comprehensive new executive compensation rules, which provide for improved disclosure of all components of executive pay and an explanation of how corporate performance relates to pay. In 1994, the Internal Revenue Service (IRS) issued rules prohibiting the tax deductibility of executive compensation of more than \$1 million. As a result, companies that wish to maintain deductibility for non-deferred compensation above the limit must now obtain shareholder approval for their incentive compensation plans, including cash bonus plans.

The IRS rules implemented the requirements of the Omnibus Budget and Reconciliation Act of 1993 (OBRA). The \$1 million compensation limit was designed to curtail rapidly inflating executive compensation and to tie more of future compensation to corporate performance. Congress enacted the law in response to years of intense public debate over the level of compensation paid to American executives.

➤ LACERA votes *case-by-case* on executive and director compensation plans (stock option plans) with the view that "viable compensation programs reward the creation of stockholder wealth by having a high payout sensitivity to increases in shareholder value"⁹.

⁹ Richard G. Peck, "Creating True Shareholder Wealth--A Compensation Idea that is Long Past Due," Management Quarterly, Volume 32, No. 1, Spring 1991, pp. 25-43.

Steps in evaluating a compensation plan:

- *Estimate the present value of all short and long-term incentives, derivative awards, and cash/bonus compensation--then assign a dollar value to the amount of potential shareholder wealth transfer.*
 - *Calculate the plan's dilutive effect both on shareholder wealth and on voting power.*
 - *Value equity-based compensation along with the cash components of pay.*
 - *Compare costs to appropriate benchmark.*
- *Factors such as re-pricing underwater stock options without shareholder approval would cause LACERA to vote **against** a plan. Additionally, in some cases we would vote against a plan deemed unnecessary.*
- *LACERA votes management proposals seeking approval to re-price options **case-by-case**. The following data is evaluated.*
- *Stock Price Volatility*
 - *Rationale*
 - *Value-for Value Exchange*
 - *Option Vesting*
 - *Term of the Option*
 - *Exercise Price*
 - *Participants*
 - *Intent*
 - *Timing*

Stock Option Expensing

- *LACERA will vote **for** the expensing of stock options, unless the company has already publicly committed to option expensing.*

Holding Period Proposals

- *LACERA will vote **for** shareholder proposals to establish required vesting periods for executive stock options.*
- *Vesting periods should be at least five years from the grant date.*
 - *Executives set to retire within three years should be prohibited from receiving stock options.*
 - *Post retirement exercise periods should be limited to no more than three years.*

Pension Fund Income

- *Earnings generated by the pension plan should not be included for executive compensation purposes.*

A. Omnibus Budget Reconciliation Act of 1987(OBRA)-Related Compensation Proposals

- **Amendments that Place a Cap on Annual Grant or Amend Administrative Features**

- *LACERA votes **for** plans that simply amend shareholder-approved plans to include administrative features or place a cap on the annual grants any one participant may receive to comply with the provisions of Section 162(m) of OBRA.*

- **Amendments to Add Performance-Based Goals**

- *LACERA votes **for** amendments to add performance goals to existing compensation plans to comply with the provisions of Section 162(m) of OBRA.*

- **Amendments to Increase Shares and Retain Tax Deductions Under OBRA**

- *Amendments to existing plans to increase shares reserved and to qualify the plan for favorable tax treatment under the provisions of Section 162(m) are evaluated **case-by-case**.*

- **Approval of Cash or Cash-and-Stock Bonus Plans**

- *LACERA votes **for** cash or cash-and-stock bonus plans to exempt the compensation from taxes under the provisions of Section 162(m) of OBRA.*

B. Employee Stock Purchase Plans

- *LACERA votes **for** proposals with (1) a purchase price at least 85 percent of the fair market value, (2) an offering period of 27 months or less and (3) a dilution of voting power less than ten percent.*

C. Shareholder Proposals to Limit Executive and Director Pay

Philosophically, LACERA believes that corporate executives should be fairly compensated for their efforts. Corporate executives contend their compensation should be based primarily on risks incurred. LACERA, however, believes that executive compensation should not be based on perceived risks because it is the stockholders, more than anyone else, who ultimately bear these risks. Moreover, executives should not expect to be compensated like top-tier entrepreneurs because generally, unlike entrepreneurs, they do not have much personal wealth at risk. Rather, the vast majority of capital at risk belongs to the corporation's shareholders.

Executive compensation should also be considered in the context of how a firm compensates its employees relative to their peers in the industry. If the firm pays their employees “bottom quartile” wages, it is difficult to justify paying their executives “top quartile” salaries.

Shareholder proposals that limit executive or director pay usually focus on the absolute dollar figure of the compensation or focus on the ratio of compensation between the executives and the average worker of a specific company. For example, at a recent annual meeting, two shareholders submitted a proposal requesting that management limit executive compensation to 20 times the pay of the average worker. Proposals are also submitted requesting that annual compensation not exceed a specified dollar figure, such as \$100,000.

Arbitrary limitations may actually hurt shareholders in the long run because management may not be able to attract and retain competent personnel. Firms forced to adhere to limits on executive compensation may find themselves at competitive disadvantage in the market for top-tier executives.

Shareholder Proposals Regarding Director Compensation

- LACERA votes ***for*** all shareholder proposals that seek additional disclosure of director pay information.
- LACERA votes ***against*** shareholder proposals seeking to set absolute levels on compensation or otherwise dictate the amount or form of compensation.
- LACERA votes ***against*** shareholder proposals requiring director fees be paid in stock only.
- LACERA reviews ***case-by-case*** all other shareholder proposals that seek to limit director pay.
- LACERA votes ***for*** proposals to place pay packages of outside directors on proxy ballots for approval by a ***majority vote of shareholders***.

Additional proxy statement disclosures supported by LACERA

- LACERA supports the inclusion of a table showing exactly what outside directors are paid, including how much is received for each type of compensation and the total pay data.

Shareholder Proposals Regarding Executive Compensation

- LACERA votes ***for*** all shareholder proposals that seek additional disclosure of executive pay information.
- LACERA votes ***against*** shareholder proposals seeking to set absolute levels on compensation or otherwise dictate the amount or form of compensation.
- LACERA votes ***for*** shareholder proposals to put option repricings to a shareholder vote.
- LACERA votes ***for*** shareholder approval of stock option plans.

- LACERA reviews case-by-case all other shareholder proposals that seek to limit executive pay.
- LACERA votes for proposals to index performance based compensation to appropriate industry peers.

Additional proxy statement disclosures supported by LACERA

- LACERA supports the requirement of a five-year graph disclosing total CEO pay versus company performance for investors.
- LACERA supports disclosure of the size of the Chief Executive Officer's total pay package.
- LACERA supports the requirement of a five-year graph showing the relationship between the annual bonus of the CEO and the company's diluted earnings per share.
- LACERA supports disclosure of the ratio of the CEO's total pay to that of an average worker in the company.
- LACERA supports disclosure of the names of compensation consultants employed by the compensation committee and by corporate management.
- LACERA supports the requirement that compensation committees must hire an independent compensation consultant and that the changing of a compensation consultant must be disclosed with the reasons for the change.
- LACERA supports disclosure of the names of comparable companies used by compensation consultants to compile pay data.
- LACERA supports disclosure of the percentile ranking of the CEO's total pay package against those of various comparable companies surveyed by the compensation consultants.
- LACERA supports disclosure of the percentile ranking for the company's five-year return versus the five-year return of the companies used in the CEO's compensation comparisons.

D. Golden and Tin Parachutes

Golden parachutes (for senior management) and tin parachutes (for middle management) are terms that describe the, often lucrative, benefits that executives receive if they are fired or quit following a change in control of their company. These benefits are frequently provided for in executives' employment contracts. They are also awarded to management by boards of directors after a company becomes the subject of takeover speculation or the actual target of a takeover attempt.

Companies rarely submit these parachute proposals to shareholders for approval. However, proposals to limit parachute payments or to require shareholder approval of parachute plans do occasionally appear on a proxy statement.

- LACERA votes for shareholder proposals to have golden and tin parachutes submitted for shareholder ratification; unless the proposal requires approval prior to entering into an employment contract.

- LACERA reviews case-by-case all proposals to ratify or cancel golden or tin parachutes.

Acceptable parachutes should:

- be less attractive than an ongoing employment opportunity with the firm
 - have a triggering mechanism beyond the control of management
 - not exceed three times base salary plus guaranteed benefits
- Severance agreements for mergers should be modified to require that the only way compensation is received is if, subsequent to a merger, the executive is fired.

Additional Proxy Statement disclosures supported by LACERA

- LACERA supports the inclusion of a table showing termination of employment payments to the CEO, including death, disability, normal retirement, discharge for cause, discharge for other than cause, and voluntary resignation.

E. Employee Stock Ownership Plans

Employee stock ownership plans (ESOPs) encourage non-management employees to acquire an ownership stake in the companies for which they work. ESOPs have been shown to promote employee loyalty and improve productivity. In addition, ESOPs offer very favorable tax treatment to corporations that adopt them, making ESOPs a very cost-effective way to fund employee retirement plans.

LACERA supports the principle of employee ownership. However, it is important to make sure that ESOPs are not being used in a way that will harm the interests of existing shareholders. The best way to ensure an ESOP is not misused by management as a takeover defense is to limit the size of the plan.

- LACERA votes for proposals that request shareholder approval to implement an ESOP or to increase authorized shares for existing ESOPs, except in cases when the number of shares allocated to the ESOP is "excessive" (i.e., generally greater than five percent of outstanding shares).

F. 401(k) Employee Benefit Plans

A 401(k) employee benefit plan is any qualified plan under Section 401 (k) of the Internal Revenue Code that contains a cash or deferred arrangement. An employee can elect to have a portion of his/her salary invested in a 401(k) plan before any income taxes are assessed (tax deferred). Because of this tax deferral, if the money is withdrawn before retirement there will be a penalty.

From a corporation's perspective, a 401(k) plan provides a highly visible benefit to employees that can be used to attract and retain quality personnel. With so many companies offering a 401(k) plan as part of a compensation/benefit package, a firm without a 401(k) plan cannot compete for quality employees in an ever-shrinking talent pool.

- LACERA votes for proposals to implement a 401(k) savings plan for employees.

G. Say-on-Pay (Advisory vote on executive compensation)

Shareholders, collectively, have limited channels to act on the information if they are dissatisfied with executive pay arrangements. Once the pay plans have been approved by management, shareholders typically do not have the ability to provide input into the execution of the plan and decisions concerning executive pay packages.

On the other hand, shareholders have the capability to withhold votes from compensation committee members. However, the effect of casting "withhold" votes is greatly diminished in cases when companies have a classified board structure and/or a plurality vote standard in place. Therefore, casting "say-on-pay" votes provides shareholders with an opportunity to voice their approval/disapproval of the executive compensation plan.

- LACERA votes case-by-case on management proposals for an advisory vote on executive compensation.
- LACERA votes against management proposals when the board has failed to demonstrate good stewardship of investors' interests regarding executive compensation practices.
- LACERA votes for shareholder proposals that recommend non-binding shareholder ratification for the compensation of the executive officers and the disclosure of information to help understand the proposed compensation package.

H. Golden Coffins

- LACERA votes case-by-case on shareholder proposals that recommend approval of payments or awards following the death of a senior executive. These payments may be in the form of unearned salary or bonuses, accelerated vesting or the continuation in force of unvested equity grants, perquisites and other payments or awards made in lieu of compensation.

I. Pay for Performance

Executive pay is often a topic of heated debate. Investors, economists, shareholders, and the media often portray executive compensation as excessive. Shareholders are especially outraged when they witness poor performance and increases in executive

pay. It is the lack of correlation between CEO pay and stock performance that lead to shareholder criticism.

Furthermore, the compensation committee often does not provide a clear explanation of the increase in pay in its reporting. The report often provides a general description of a CEO's performance and it lacks specific quantitative or qualitative assessments for shareholders to understand the increase in compensation.

- LACERA votes case-by-case on shareholder proposals that request approval of a significant amount of performance-based incentive compensation to senior executives.
- LACERA votes case-by-case on proposals advocating the use of performance based equity awards, such as performance contingent options or restricted stock, indexed options or premium-priced options.

J. Supplemental Executive Retirement Plans (SERPs)

Supplemental Executive Retirement Plans (SERPs), are executive-only retirement plans designed as a supplement to employee-wide plans. SERPs can be either defined benefit plans or a defined contribution plan. SERPs are often viewed as discriminatory because participating executives, who are selected by the company, may receive better benefit formulas than the employee-wide plan. To ensure fairness, shareholders should be able to approve SERP plans.

- LACERA votes for shareholder proposals requesting approval of SERP agreements, unless the company's executive pension plans do not contain excessive benefits.

VII. State of Incorporation

- A. Voting on State Takeover Statutes
- B. Voting on Control Share Acquisition Statutes
- C. Voting on Control Share Cash out Statutes
- D. Voting on Freezeout Provisions
- E. Voting on Fair Price Provisions
- F. Voting on Disgorgement Provisions
- G. Voting on Reincorporation Proposals

VII. State of Incorporation

The United States Constitution provides that each state must respect the legal creations of each other state. Accordingly, a company incorporated in one state is entitled to do business, and have its governance provisions respected, throughout the country.

The ability of corporations to choose a place to incorporate and establish residence has resulted in competition among many states for incorporation licensing and legal fees. Delaware has been the most successful in attracting business, with more than 50% of S&P 500 companies incorporated in the state.

The fact that approximately 20% of Delaware's public revenue is derived from incorporation fees and business taxes indicates that states benefit from formulating laws friendly to corporate management. These laws, as expected, are favorable to management by including takeover defense provisions that protect the jobs of management.

A. Voting on State Takeover Statutes

While shareholders have minimal direct control over a state's adoption of anti-takeover legislation, they may influence whether or not a company chooses to be governed by such legislation. Most state anti-takeover provisions allow companies to "opt in" or "opt out" of coverage by stating their intentions in their charters. As a result, shareholders are sometimes requested to vote on whether a company will be governed by specific state statutes.

- LACERA reviews *case-by-case* proposals to opt in or out of state takeover statutes.

B. Voting on Control Share Acquisition Statutes

Control share acquisition statutes function by denying shares their voting rights when they contribute to ownership in excess of certain thresholds. Voting rights may only be restored by approval, of either a majority or supermajority, of disinterested shares.

- LACERA votes *case-by-case* proposals to opt out of control share acquisition statutes.

C. Voting on Control Share Cash-Out Statutes

Control share cash-out statutes give dissident shareholders the right to "cash-out" of their position in a company. When an investor crosses a preset threshold level (often 20% to 25%,) remaining shareholders are given the right to sell their shares to the acquirer, who is required to buy them at the highest acquiring price.

- LACERA votes case-by-case proposals to opt out of control share cash-out statutes.

D. Voting on Freezeout Provisions

Freezeout provisions force an acquirer to wait a specific period of time, typically 2 to 5 years, before gaining control of a company. The acquirer must secure adequate financing before proceeding with the acquisition and is often also subject to a fair price requirement once the freezeout period has expired. This provision is typically utilized to prevent a highly leveraged take over, with a subsequent “break-up” and sell off of the acquired companies assets.

- LACERA votes case-by-case proposals to opt out of freezeout provisions.

E. Voting on Fair Price Provisions

Fair price provisions require anyone wishing to purchase control of a company to pay all shareholders a defined fair price. A fair price is usually defined as the highest price that a potential acquirer pays to any shareholder during a specified period of time. Fair price requirements are intended to deter two-tiered, front-end-loaded tender offers, in which shareholders that tender (sell) their shares first receive a higher price for their shares than other shareholders. State sponsored fair price statutes allow the requirement to be bypassed should a certain percentage of shareholders favor such a course of action. (Greater than 50% of states employing fair price provisions require a majority of disinterested shares, while approximately 40% require that a supermajority of all shares approve the acquisition.)

- LACERA votes case-by-case proposals to opt out of state fair price provisions.

F. Voting on Disgorgement provisions

An acquirer of more than a specified percentage of a company’s stock must pay back, to the company, any profits realized from the sale of that company’s stock purchased 24 months before achieving control status. Disgorgement provisions prevent a hostile acquirer from profiting by purchasing a large stake in a company, announcing a battle for control of that company and then selling out at the higher market price resulting from news of the potential acquisition.

- LACERA votes case-by-case proposals to opt out of disgorgement provisions.

G. Voting on Reincorporation Proposals

Re-incorporation refers to changing a company's state of incorporation. A company that reincorporates must obtain shareholder approval for the move and for the new

charter it adopts when it shifts to the new state. Many re-incorporations involve moves to Delaware to take advantage of Delaware's flexible corporate laws.

A re-incorporation proposal is sometimes part of a restructuring effort or merger agreement. As such, its contribution to a company's growth, financial health and competitive position can outweigh the anticipated negative consequences of incorporating in states with many anti-takeover statutes. Re-incorporations can also result in lower taxes and incorporation fees. In addition, there may be advantages to reincorporating in the state in which the company conducts the bulk of its business.

- LACERA examines proposals to change a company's state of incorporation **case-by-case** giving consideration to both financial and corporate governance concerns:
 - Reasons for re-incorporation.
 - Comparison of company's governance provisions prior to and following the transaction.
 - Comparison of corporation laws of original state and destination state.
- LACERA votes **for** re-incorporation when the economic factors outweigh any neutral or negative governance changes.

VIII. Mergers and Corporate Restructuring

- A. Mergers and acquisitions
- B. Corporate Restructuring
- C. Spin-offs
- D. Asset Sales
- E. Liquidations
- F. Appraisal Rights
- G. Changing Corporate Name
- H. Amending Bylaws

VIII. Mergers and Corporate Restructuring

Mergers and corporate restructuring have major financial implications for shareholders. Many of these transactions require shareholder approval. LACERA carefully examines each proposal to determine whether it is in the best financial interests of the shareholders.

The fact that a proposed transaction would provide an above market premium to shareholders is one relevant factor in making a voting decision. However, the offer of a premium does not necessarily mean the transaction is in a shareholder's best interest.

Sometimes these transactions include provisions that LACERA would oppose (anti-takeover measures, for example) if given the opportunity to vote separately on all the provisions. But when the transaction is presented as a single package, the voting decision must be made on the basis of whether the entire proposal is in LACERA's best interest. This requires an analysis of all relevant facts and circumstances.

A. Mergers and Acquisitions

When one company merges with or is acquired by another, the company's board of directors often recommends the merger or acquisition agreement and submits the proposal to shareholders for approval. If the board does not approve the merger or acquisition, but the hostile tender offer is successful, a shareholder vote on the proposal may also occur.

➤ *LACERA, in conjunction with RMG, evaluates mergers and acquisitions case-by-case taking into account the following:*

- Valuation – Is the value to be received by the target shareholders (or paid by the acquirer) reasonable? The fairness opinion provides an initial starting point for assessing valuation reasonableness, but RMG also places emphasis on the offer premium, market reaction and strategic rationale.
- Market reaction – How has the market responded to the proposed deal? A negative market reaction will cause RMG to scrutinize a deal more closely.
- Strategic rationale – Does the deal make sense strategically? From where is the value derived? Cost and revenue synergies should not be overly aggressive or optimistic, but reasonably achievable. Management should also have a favorable track record of successful integration of historical acquisitions.
- Negotiations and process – Were the terms of the transaction negotiated at arm's-length? Was the process fair and equitable? A fair process helps to ensure the best price for shareholders. Significant negotiation “wins” can also signify the deal makers’ competency. How the target was shopped

- (e.g., full auction, partial auction, no auction) can also affect shareholder value.
- Conflicts of interest - Are insiders benefiting from the transaction disproportionately and inappropriately as compared to non-insider shareholders? As the result of potential conflicts, the directors and officers of the company may be more likely to vote to approve a merger than if they did not hold these interests.
 - Governance - Will the combined company have a better or worse governance profile than the respective current governance profiles of the respective parties to the transaction? If the governance profile is to change for the worse, the burden is on the company to prove that other issues (such as valuation) outweigh any deterioration in governance.

B. Corporate Restructuring

In certain business situations, majority shareholders of a corporation desire to gain complete control of the assets and cash flow of a company. To accomplish this task called "taking a public company private", it is necessary for the majority shareholders to eliminate the minority shareholders. The two principal means for taking a public company private are through minority squeeze-outs and leveraged buyouts (LBO). However, most of the proposals presented to shareholders for approval are specifically management-sponsored LBO's.

- *Corporate restructuring proposals, including leveraged buyouts and squeeze-outs, are evaluated **case-by-case**.*

Squeeze-out

- *Minority shareholders faced with a squeeze-out situation should evaluate the fairness of the offer price.*
- *Fairness opinions should be scrutinized as in merger situations.*

Leveraged Buyouts (LBOs)

- *Review offer price for substantial premium, reflective of the value created by the transfer of control from agents to principals.*
- *In addition to assessing the premium offered in a leveraged buy out, shareholders should also weigh the costs of not approving the transaction, as shareholders will be left bearing the cost of a failed LBO.*

C. Spin-offs

One of the more popular and successful corporate strategy developed in recent years is the spin-off of a segment or division of a large corporation to its shareholders as a separate corporate entity. If approved, spin-off shares are sent out to existing investors as a bonus or a dividend share. As long as there is a legitimate business purpose for the

spin-off, rather than mere tax avoidance, Section 355 of the Internal Revenue Code declares that spin-offs are tax-free (as long as the stock is held).

- *Spin-offs are evaluated case-by-case depending on the tax and regulatory advantages, planned use of sale proceeds, managerial incentives, valuation of spinoff, fairness opinion, benefits to the parent company, conflicts of interest, corporate governance changes, and changes in the capital structure.*

D. Asset Sales

Corporations cite many reasons for divesting corporate assets, including the need to raise capital, getting rid of an unprofitable business, and repayment of debt. However, the two main reasons for the sale of a corporate asset are: 1) the asset in question is causing "diseconomies" of scale or negative synergies, i.e., the asset is not only failing to generate adequate returns, but is also harming the value of the company as a whole and, 2) the company simply thinks it can sell the asset for a large gain to a buyer who can make better use of the asset.

- *LACERA votes case-by-case on asset sales after evaluating the impact on the balance sheet/working capital, value received for the asset, potential elimination of diseconomies, anticipated financial and operating benefits, anticipated use of funds, fairness opinion, how the deal was negotiated, and conflicts of interest.*

E. Liquidations

Liquidation proposals are generally bad news for long-term investors. They usually occur after a prolonged period of declines in earnings and share prices. However, liquidation may be an attractive option if the sale of the firm's assets on a piece-meal basis can be accomplished at a higher than market price.

- *LACERA votes for/against liquidations case-by-case after reviewing management's efforts to pursue other alternatives, appraised value of assets, and the compensation plan for executives managing the liquidation. It is critical to review the likelihood that the company will file for bankruptcy, if the liquidation proposal is not approved.*

F. Appraisal Rights

Rights of appraisal provide shareholders who are not satisfied with the terms of certain corporate transactions, such as a merger or corporate re-structuring, the right to demand a judicial review of the transaction to determine a fair market value for their shares.

- *LACERA votes for proposals to restore, or provide shareholders with, rights of appraisal.*

G. Changing Corporate Name

Although this corporate action may seem insignificant, one empirical study has shown that name changes which are distinctive, or are more functional than the original name have a positive effect on stock prices¹⁰. Furthermore, when considering that management has just spent a large sum on the selection of a new name, it's probably better to vote for the proposed name before management goes back to the drawing board and spends another large amount attempting to again change the name.

- LACERA votes for changing a corporation's name.

H. Amending Bylaws

- LACERA votes against proposals giving the board exclusive authority to amend the bylaws.
- LACERA votes for proposals giving the board the ability to amend the bylaws subject to shareholders approval.

¹⁰ Linda J. Morris, Mario G.C. Reyes, "Corporate Name Changes: The Association Between Functional Name Characteristics and Stock Performance, "Journal of Applied Business Research, Vol. 8, Winter 1991-92, pp. 110-17.

IX. Auditors

IX. Auditors

Ratifying Auditors

Companies are not legally required to allow shareholders to ratify the selection of auditors; therefore, sometimes shareholders are not given an opportunity to vote on ratification of an auditor. However, even if not required, many companies seek shareholder ratification of auditors.

Companies typically disclose the audit firm retained, and ask for shareholder approval. Occasionally, companies also assert in the proxy statement that if shareholders do not ratify the selection of auditors, the board will consider switching to a new auditor.

- LACERA votes **for** proposals to ratify auditors, unless an auditor has a financial interest in or association with the company and is therefore not independent; or there is reason to believe that the independent auditor has rendered an opinion, which is neither accurate nor indicative of the company's financial position.

Non Audit Fees / Auditor Independence

- LACERA will vote **against** auditors and withhold votes from Audit Committee members if: Non-audit ("other") fees > audit fees + audit-related fees + permissible tax fees.
- LACERA will vote **case-by-case** on shareholder proposals limiting non-audit services, evaluating whether non-audit services are excessive and whether the company has policies in place to limit non-audit services or prevent conflicts of interest.

Auditor Firm Rotation

- LACERA votes **for** proposals to rotate audit firms unless the rotation period is less than five years.

- X. **Social and Environmental Issues**
 - A. Social and Environmental

X. Social and Environmental Issues

A. Social and Environmental

Although social responsibility proposals are seldom approved by shareholders, they focus shareholders and management attention on public issues related to a corporation's business activities. Even though the impact of these proposals on sales, earnings and return to shareholders is insignificant, careful attention to these issues has the potential to be beneficial to corporations and their shareholders.

It is good business for corporations to be responsive to public expectations. Conversely, a corporation that ignores the social impact of its activities does so at its own risk. Therefore, it is in the corporation's best interest, and the best interests of its shareholders, to carefully consider the impact that a company's business activities have on the public.

On November 19, 2008, LACERA's Board of Investments adopted the United Nations Principles for Responsible Investment, a set of global best practices for social, environmental and governance (ESG) investing. RiskMetrics Group (RMG) is also a signatory to the Principles. As a result, RMG incorporates the relevant aspects of the Principles into its proxy analysis process. Therefore, when considering how to vote on ESG proposals, investment staff relies on the research expertise and voting recommendations of RMG.¹¹

- *LACERA, in conjunction with RMG, votes case-by-case on shareholder social and environmental proposals, on the basis that their impact on share value can rarely be anticipated with any high degree of confidence.*

In many cases, however, LACERA votes for disclosure reports that seek additional information, particularly when it appears companies have not adequately addressed shareholders' social and environmental concerns.

When voting on shareholder social and environmental proposals, RMG analyzes the following factors:

- Whether adoption of the proposal would have either a positive or negative impact on the company's short-term or long-term share value;
- The percentage of sales, assets and earnings affected;

¹¹ RiskMetrics Group, formerly Institutional Shareholder Services (ISS), has provided LACERA with global proxy advisory services since 1991. They became a signatory to the Principles in January 2008.

- The degree to which the company's stated position on the issues could affect its reputation or sales, or leave it vulnerable to boycott or selective purchasing;
- Whether the issues presented should be dealt with through government or company-specific action;
- Whether the company has already responded in some appropriate manner to the request embodied in a proposal;
- Whether the company's analysis and voting recommendation to shareholders is persuasive;
- What other companies have done in response to the issue;
- Whether the proposal itself is well framed and reasonable;
- Whether implementation of the proposal would achieve the objectives sought in the proposal; and
- Whether the subject of the proposal is best left to the discretion of the board.

Examples of the social and environmental issues to which this type of analysis is applied:

- Climate Change and Environment
- Military Business
- World Debt Crisis
- Product Integrity and Marketing
- Human Rights and Labor Standards
- Animal Welfare
- Sustainability Reporting

XI. Other Issues

A. Corporate Governance Committee

The Board of Investments has delegated certain responsibilities to the Corporate Governance Committee, as set forth in the Corporate Governance Committee Policy Statement.

1. Shareholder Proposals Involving Issues Not Addressed in Sections I through X

The Corporate Governance Committee is authorized to instruct the investment staff to cast votes on shareholder proposals for which guidelines are not provided in Sections I through X, provided the proposal is sponsored by an institutional investor or group of institutional investors owning at least 5% of the outstanding shares of the corporation. All such votes shall be in accordance with the Corporate Governance Principles approved by the Board of Investments. The Committee shall provide each member of the Board of Investments with written notice of its instructions to vote proxies no later than the business day immediately following the day instructions were issued. Such notice shall include:

- A brief summary of the proposal.
- The sponsor or sponsors of the proposal.
- The vote cast.
- The Corporate Governance Principle(s) that support the vote.
- The RMG recommendation on the proposal, if any, and if a contrary vote is cast, the basis for not adopting the RMG recommendation.
- The recommendation of LACERA active managers holding the security, if any.
- The CII recommendation on the proposal, if any.

2. Recommending Votes Contrary to the Established Proxy Voting Guidelines

The Corporate Governance Committee may, in appropriate cases, recommend to the Board of Investments that votes be cast on a particular issue contrary to the Board's established Proxy Voting Guidelines. Votes may not be cast contrary to the Guidelines unless duly authorized by the Board.